

108TH CONGRESS
1ST SESSION

H. R. 44

To amend the Internal Revenue Code of 1986 to provide reduced capital gain rates for qualified economic stimulus gain and to index the basis of assets of individuals for purposes of determining gains and losses.

IN THE HOUSE OF REPRESENTATIVES

JANUARY 7, 2003

Mr. DREIER (for himself, Mr. HALL, Ms. DUNN, Ms. MCCARTHY of Missouri, Mr. ENGLISH, Mr. SESSIONS, Mr. TOOMEY, and Mr. MANZULLO) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to provide reduced capital gain rates for qualified economic stimulus gain and to index the basis of assets of individuals for purposes of determining gains and losses.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE, ETC.**

4 (a) SHORT TITLE.—This Act may be cited as the
5 “Investment Tax Incentive Act of 2003”.

6 (b) AMENDMENT OF 1986 CODE.—Except as other-
7 wise expressly provided, whenever in this Act an amend-

1 ment or repeal is expressed in terms of an amendment
 2 to, or repeal of, a section or other provision, the reference
 3 shall be considered to be made to a section or other provi-
 4 sion of the Internal Revenue Code of 1986.

5 **SEC. 2. REDUCED CAPITAL GAIN RATES FOR QUALIFIED**
 6 **ECONOMIC STIMULUS GAIN.**

7 (a) MAXIMUM CAPITAL GAIN RATE FOR INDIVID-
 8 UALS.—

9 (1) IN GENERAL.—Paragraph (2) of section
 10 1(h) (relating to reduced capital gain rates for quali-
 11 fied 5-year gain) is amended to read as follows:

12 “(2) REDUCED CAPITAL GAIN RATES FOR
 13 QUALIFIED 5-YEAR GAIN, QUALIFIED ECONOMIC
 14 STIMULUS GAIN, AND QUALIFIED SECTION 1202 ECO-
 15 NOMIC STIMULUS GAIN.—

16 “(A) REDUCTION IN 10-PERCENT RATE.—

17 The rate under paragraph (1)(B) shall be—

18 “(i) 5 percent with respect to so much
 19 of the amount to which the 10-percent rate
 20 would otherwise apply as does not exceed
 21 qualified economic stimulus gain,

22 “(ii) 8 percent with respect to so
 23 much of such amount not taken into ac-
 24 count under clause (i) as does not exceed
 25 qualified 5-year gain, and

1 “(iii) 10 percent with respect to the
2 remainder of such amount.

3 “(B) REDUCTION IN 20-PERCENT RATE.—

4 The rate under paragraph (1)(C) shall be—

5 “(i) 10 percent with respect to so
6 much of the amount to which the 20-per-
7 cent rate would otherwise apply as does
8 not exceed the excess of qualified economic
9 stimulus gain over the amount of such
10 gain taken into account under subpara-
11 graph (A)(i),

12 “(ii) 18 percent with respect to so
13 much of such amount not taken into ac-
14 count under clause (i) as does not exceed
15 the lesser of—

16 “(I) the excess of qualified 5-year
17 gain over the amount of such gain
18 taken into account under subpara-
19 graph (A)(ii), or

20 “(II) the amount of qualified 5-
21 year gain (determined by taking into
22 account only property the holding pe-
23 riod for which begins after December
24 31, 2000), and

1 “(iii) 20 percent with respect to the
2 remainder of such amount.

3 For purposes of determining under clause
4 (ii)(II) whether the holding period of property
5 begins after December 31, 2000, the holding
6 period of property acquired pursuant to the ex-
7 ercise of an option (or other right or obligation
8 to acquire property) shall include the period
9 such option (or other right or obligation) was
10 held.

11 “(C) REDUCTION IN 28-PERCENT RATE.—
12 The rate under paragraph (1)(E) shall be—

13 “(i) 14 percent with respect to so
14 much of the amount to which the 28-per-
15 cent rate would otherwise apply as does
16 not exceed qualified section 1202 economic
17 stimulus gain, and

18 “(ii) 28 percent with respect to the re-
19 mainder of such amount.”.

20 (2) QUALIFIED ECONOMIC STIMULUS GAIN;
21 QUALIFIED SECTION 1202 ECONOMIC STIMULUS
22 GAIN.—Subsection (h) of section 1 (relating to max-
23 imum capital gains rate) is amended by adding at
24 the end the following new paragraphs:

1 “(13) QUALIFIED ECONOMIC STIMULUS GAIN.—

2 For purposes of this subsection, the term ‘qualified
3 economic stimulus gain’ means the aggregate long-
4 term capital gain from property the holding period
5 for which begins during the 2-year period beginning
6 on the date of the enactment of this paragraph. The
7 determination under the preceding sentence shall be
8 made without regard to collectibles gain, gain de-
9 scribed in paragraph (7)(A)(i), and section 1202
10 gain.

11 “(14) QUALIFIED SECTION 1202 ECONOMIC
12 STIMULUS GAIN.—For purposes of this subsection,
13 the term ‘qualified section 1202 economic stimulus
14 gain’ means the aggregate section 1202 gain from
15 property the holding period for which begins during
16 the 2-year period beginning on the date of the enact-
17 ment of this paragraph.”.

18 (3) EXCLUSION OF QUALIFIED ECONOMIC STIM-
19 ULUS GAIN FROM QUALIFIED 5-YEAR GAIN.—Para-
20 graph (9) of section 1(h) is amended by inserting
21 “qualified economic stimulus gain,” before “collect-
22 ibles gain”.

23 (b) MAXIMUM CAPITAL GAIN RATE FOR CORPORA-
24 TIONS.—Section 1201 is amended to read as follows:

1 **“SEC. 1201. ALTERNATIVE TAX FOR CORPORATIONS.**

2 “(a) GENERAL RULE.—If for any taxable year a cor-
 3 poration has a qualified economic stimulus gain, then, in
 4 lieu of any tax imposed by sections 11, 511, and 831(a)
 5 and (b), there is hereby imposed a tax (if such tax is less
 6 than the tax imposed by such sections) which shall consist
 7 of the sum of—

8 “(1) a tax computed on the taxable income re-
 9 duced by the amount of qualified economic stimulus
 10 gain, at the rates and in the manner as if this sub-
 11 section had not been enacted, plus

12 “(2) a tax of 20 percent of the qualified eco-
 13 nomic stimulus gain (or, if less, taxable income).

14 “(b) QUALIFIED ECONOMIC STIMULUS GAIN.—For
 15 purposes of this section, the term ‘qualified economic stim-
 16 ulus gain’ has the meaning given such term in section
 17 1(h)(13), except that such gain shall not exceed the net
 18 capital gain.

19 “(c) REGULATIONS.—Rules similar to the rules of
 20 section 1(h)(11) shall apply for purposes of this section.

21 “(d) CROSS REFERENCES.—

“For computation of the alternative tax—

**“(1) in the case of life insurance companies, see
 section 801(a)(2),**

**“(2) in the case of regulated investment compa-
 nies and their shareholders, see section 852(b)(3)(A)
 and (D), and**

**“(3) in the case of real estate investment trusts,
 see section 857(b)(3)(A).”**

1 (c) CONFORMING AMENDMENT.—Section
 2 857(b)(3)(A)(ii) is amended by striking “determined at
 3 the rate provided in section 1201(a)” and inserting “, de-
 4 termined as provided in section 1201(a),”.

5 (d) EFFECTIVE DATE.—The amendments made by
 6 this section shall apply to taxable years beginning after
 7 the date of the enactment of this Act.

8 **SEC. 3. INDEXING OF CERTAIN ASSETS FOR PURPOSES OF**
 9 **DETERMINING GAIN OR LOSS.**

10 (a) IN GENERAL.—Part II of subchapter O of chap-
 11 ter 1 (relating to basis rules of general application) is
 12 amended by redesignating section 1023 as section 1024
 13 and by inserting after section 1022 the following new sec-
 14 tion:

15 **“SEC. 1023. INDEXING OF CERTAIN ASSETS FOR PURPOSES**
 16 **OF DETERMINING GAIN OR LOSS.**

17 **“(a) GENERAL RULE.—**

18 **“(1) INDEXED BASIS SUBSTITUTED FOR AD-**
 19 **JUSTED BASIS.—**Solely for purposes of determining
 20 gain or loss on the sale or other disposition by a tax-
 21 payer (other than a corporation) of an indexed asset
 22 which has been held for more than 3 years, the in-
 23 dexed basis of the asset shall be substituted for its
 24 adjusted basis.

1 “(2) EXCEPTION FOR DEPRECIATION, ETC.—

2 The deductions for depreciation, depletion, and am-
3 ortization shall be determined without regard to the
4 application of paragraph (1) to the taxpayer or any
5 other person.

6 “(b) INDEXED ASSET.—

7 “(1) IN GENERAL.—For purposes of this sec-
8 tion, the term ‘indexed asset’ means—

9 “(A) common stock in a C corporation
10 (other than a foreign corporation), and

11 “(B) tangible property,
12 which is a capital asset or property used in the trade
13 or business (as defined in section 1231(b)).

14 “(2) STOCK IN CERTAIN FOREIGN CORPORA-
15 TIONS INCLUDED.—For purposes of this section—

16 “(A) IN GENERAL.—The term ‘indexed
17 asset’ includes common stock in a foreign cor-
18 poration which is regularly traded on an estab-
19 lished securities market.

20 “(B) EXCEPTION.—Subparagraph (A)
21 shall not apply to—

22 “(i) stock of a foreign investment
23 company (within the meaning of section
24 1246(b)),

1 “(ii) stock in a passive foreign invest-
 2 ment company (as defined in section
 3 1296),

4 “(iii) stock in a foreign corporation
 5 held by a United States person who meets
 6 the requirements of section 1248(a)(2),
 7 and

8 “(iv) stock in a foreign personal hold-
 9 ing company (as defined in section 552).

10 “(C) TREATMENT OF AMERICAN DEPOSI-
 11 TORY RECEIPTS.—An American depository re-
 12 ceipt for common stock in a foreign corporation
 13 shall be treated as common stock in such cor-
 14 poration.

15 “(c) INDEXED BASIS.—For purposes of this sec-
 16 tion—

17 “(1) GENERAL RULE.—The indexed basis for
 18 any asset is—

19 “(A) the adjusted basis of the asset, in-
 20 creased by

21 “(B) the applicable inflation adjustment.

22 “(2) APPLICABLE INFLATION ADJUSTMENT.—
 23 The applicable inflation adjustment for any asset is
 24 an amount equal to—

1 “(A) the adjusted basis of the asset, multi-
2 plied by

3 “(B) the percentage (if any) by which—

4 “(i) the gross domestic product
5 deflator for the last calendar quarter end-
6 ing before the asset is disposed of, exceeds

7 “(ii) the gross domestic product
8 deflator for the last calendar quarter end-
9 ing before the asset was acquired by the
10 taxpayer (or, if later, the calendar quarter
11 ending on December 31, 2002).

12 The percentage under subparagraph (B) shall be
13 rounded to the nearest $\frac{1}{10}$ of 1 percentage point.

14 “(3) GROSS DOMESTIC PRODUCT DEFLATOR.—

15 The gross domestic product deflator for any cal-
16 endar quarter is the implicit price deflator for the
17 gross domestic product for such quarter (as shown
18 in the last revision thereof released by the Secretary
19 of Commerce before the close of the following cal-
20 endar quarter).

21 “(d) SUSPENSION OF HOLDING PERIOD WHERE DI-
22 MINISHED RISK OF LOSS; TREATMENT OF SHORT
23 SALES.—

24 “(1) IN GENERAL.—If the taxpayer (or a re-
25 lated person) enters into any transaction which sub-

1 stantially reduces the risk of loss from holding any
2 asset, such asset shall not be treated as an indexed
3 asset for the period of such reduced risk.

4 “(2) SHORT SALES.—

5 “(A) IN GENERAL.—In the case of a short
6 sale of an indexed asset with a short sale period
7 in excess of 3 years, for purposes of this title,
8 the amount realized shall be an amount equal
9 to the amount realized (determined without re-
10 gard to this paragraph) increased by the appli-
11 cable inflation adjustment. In applying sub-
12 section (c)(2) for purposes of the preceding sen-
13 tence, the date on which the property is sold
14 short shall be treated as the date of acquisition
15 and the closing date for the sale shall be treat-
16 ed as the date of disposition.

17 “(B) SHORT SALE PERIOD.—For purposes
18 of subparagraph (A), the short sale period be-
19 gins on the day that the property is sold and
20 ends on the closing date for the sale.

21 “(e) TREATMENT OF REGULATED INVESTMENT
22 COMPANIES AND REAL ESTATE INVESTMENT TRUSTS.—

23 “(1) ADJUSTMENTS AT ENTITY LEVEL.—

24 “(A) IN GENERAL.—Except as otherwise
25 provided in this paragraph, the adjustment

1 under subsection (a) shall be allowed to any
2 qualified investment entity (including for pur-
3 poses of determining the earnings and profits of
4 such entity).

5 “(B) EXCEPTION FOR CORPORATE SHARE-
6 HOLDERS.—Under regulations—

7 “(i) in the case of a distribution by a
8 qualified investment entity (directly or in-
9 directly) to a corporation—

10 “(I) the determination of whether
11 such distribution is a dividend shall be
12 made without regard to this section,
13 and

14 “(II) the amount treated as gain
15 by reason of the receipt of any capital
16 gain dividend shall be increased by the
17 percentage by which the entity’s net
18 capital gain for the taxable year (de-
19 termined without regard to this sec-
20 tion) exceeds the entity’s net capital
21 gain for such year determined with re-
22 gard to this section, and

23 “(ii) there shall be other appropriate
24 adjustments (including deemed distribu-
25 tions) so as to ensure that the benefits of

1 this section are not allowed (directly or in-
2 directly) to corporate shareholders of quali-
3 fied investment entities.

4 For purposes of the preceding sentence, any
5 amount includible in gross income under section
6 852(b)(3)(D) shall be treated as a capital gain
7 dividend and an S corporation shall not be
8 treated as a corporation.

9 “(C) EXCEPTION FOR QUALIFICATION
10 PURPOSES.—This section shall not apply for
11 purposes of sections 851(b) and 856(e).

12 “(D) EXCEPTION FOR CERTAIN TAXES IM-
13 POSED AT ENTITY LEVEL.—

14 “(i) TAX ON FAILURE TO DISTRIBUTE
15 ENTIRE GAIN.—If any amount is subject to
16 tax under section 852(b)(3)(A) for any
17 taxable year, the amount on which tax is
18 imposed under such section shall be in-
19 creased by the percentage determined
20 under subparagraph (B)(i)(II). A similar
21 rule shall apply in the case of any amount
22 subject to tax under paragraph (2) or (3)
23 of section 857(b) to the extent attributable
24 to the excess of the net capital gain over
25 the deduction for dividends paid deter-

1 mined with reference to capital gain divi-
 2 dends only. The first sentence of this
 3 clause shall not apply to so much of the
 4 amount subject to tax under section
 5 852(b)(3)(A) as is designated by the com-
 6 pany under section 852(b)(3)(D).

7 “(ii) OTHER TAXES.—This section
 8 shall not apply for purposes of determining
 9 the amount of any tax imposed by para-
 10 graph (4), (5), or (6) of section 857(b).

11 “(2) ADJUSTMENTS TO INTERESTS HELD IN
 12 ENTITY.—

13 “(A) REGULATED INVESTMENT COMPA-
 14 NIES.—Stock in a regulated investment com-
 15 pany (within the meaning of section 851) shall
 16 be an indexed asset for any calendar quarter in
 17 the same ratio as—

18 “(i) the average of the fair market
 19 values of the indexed assets held by such
 20 company at the close of each month during
 21 such quarter, bears to

22 “(ii) the average of the fair market
 23 values of all assets held by such company
 24 at the close of each such month.

1 “(B) REAL ESTATE INVESTMENT
 2 TRUSTS.—Stock in a real estate investment
 3 trust (within the meaning of section 856) shall
 4 be an indexed asset for any calendar quarter in
 5 the same ratio as—

6 “(i) the fair market value of the in-
 7 dexed assets held by such trust at the close
 8 of such quarter, bears to

9 “(ii) the fair market value of all as-
 10 sets held by such trust at the close of such
 11 quarter.

12 “(C) RATIO OF 80 PERCENT OR MORE.—If
 13 the ratio for any calendar quarter determined
 14 under subparagraph (A) or (B) would (but for
 15 this subparagraph) be 80 percent or more, such
 16 ratio for such quarter shall be 100 percent.

17 “(D) RATIO OF 20 PERCENT OR LESS.—If
 18 the ratio for any calendar quarter determined
 19 under subparagraph (A) or (B) would (but for
 20 this subparagraph) be 20 percent or less, such
 21 ratio for such quarter shall be zero.

22 “(E) LOOK-THRU OF PARTNERSHIPS.—For
 23 purposes of this paragraph, a qualified invest-
 24 ment entity which holds a partnership interest
 25 shall be treated (in lieu of holding a partnership

1 interest) as holding its proportionate share of
2 the assets held by the partnership.

3 “(3) TREATMENT OF RETURN OF CAPITAL DIS-
4 TRIBUTIONS.—Except as otherwise provided by the
5 Secretary, a distribution with respect to stock in a
6 qualified investment entity which is not a dividend
7 and which results in a reduction in the adjusted
8 basis of such stock shall be treated as allocable to
9 stock acquired by the taxpayer in the order in which
10 such stock was acquired.

11 “(4) QUALIFIED INVESTMENT ENTITY.—For
12 purposes of this subsection, the term ‘qualified in-
13 vestment entity’ means—

14 “(A) a regulated investment company
15 (within the meaning of section 851), and

16 “(B) a real estate investment trust (within
17 the meaning of section 856).

18 “(f) OTHER PASS-THRU ENTITIES.—

19 “(1) PARTNERSHIPS.—

20 “(A) IN GENERAL.—In the case of a part-
21 nership, the adjustment made under subsection
22 (a) at the partnership level shall be passed
23 through to the partners.

24 “(B) SPECIAL RULE IN THE CASE OF SEC-
25 TION 754 ELECTIONS.—In the case of a transfer

1 of an interest in a partnership with respect to
2 which the election provided in section 754 is in
3 effect—

4 “(i) the adjustment under section
5 743(b)(1) shall, with respect to the trans-
6 feror partner, be treated as a sale of the
7 partnership assets for purposes of applying
8 this section, and

9 “(ii) with respect to the transferee
10 partner, the partnership’s holding period
11 for purposes of this section in such assets
12 shall be treated as beginning on the date
13 of such adjustment.

14 “(2) S CORPORATIONS.—In the case of an S
15 corporation, the adjustment made under subsection
16 (a) at the corporate level shall be passed through to
17 the shareholders. This section shall not apply for
18 purposes of determining the amount of any tax im-
19 posed by section 1374 or 1375.

20 “(3) COMMON TRUST FUNDS.—In the case of a
21 common trust fund, the adjustment made under sub-
22 section (a) at the trust level shall be passed through
23 to the participants.

24 “(4) INDEXING ADJUSTMENT DISREGARDED IN
25 DETERMINING LOSS ON SALE OF INTEREST IN ENTI-

1 TY.—Notwithstanding the preceding provisions of
 2 this subsection, for purposes of determining the
 3 amount of any loss on a sale or exchange of an in-
 4 terest in a partnership, S corporation, or common
 5 trust fund, the adjustment made under subsection
 6 (a) shall not be taken into account in determining
 7 the adjusted basis of such interest.

8 “(g) DISPOSITIONS BETWEEN RELATED PERSONS.—

9 “(1) IN GENERAL.—This section shall not apply
 10 to any sale or other disposition of property between
 11 related persons except to the extent that the basis
 12 of such property in the hands of the transferee is a
 13 substituted basis.

14 “(2) RELATED PERSONS DEFINED.—For pur-
 15 poses of this section, the term ‘related persons’
 16 means—

17 “(A) persons bearing a relationship set
 18 forth in section 267(b), and

19 “(B) persons treated as single employer
 20 under subsection (b) or (c) of section 414.

21 “(h) TRANSFERS TO INCREASE INDEXING ADJUST-
 22 MENT.—If any person transfers cash, debt, or any other
 23 property to another person and the principal purpose of
 24 such transfer is to secure or increase an adjustment under

1 subsection (a), the Secretary may disallow part or all of
2 such adjustment or increase.

3 “(i) SPECIAL RULES.—For purposes of this section—

4 “(1) TREATMENT OF IMPROVEMENTS, ETC.—If
5 there is an addition to the adjusted basis of any tan-
6 gible property or of any stock in a corporation dur-
7 ing the taxable year by reason of an improvement to
8 such property or a contribution to capital of such
9 corporation—

10 “(A) such addition shall never be taken
11 into account under subsection (c)(1)(A) if the
12 aggregate amount thereof during the taxable
13 year with respect to such property or stock is
14 less than \$1,000, and

15 “(B) such addition shall be treated as a
16 separate asset acquired at the close of such tax-
17 able year if the aggregate amount thereof dur-
18 ing the taxable year with respect to such prop-
19 erty or stock is \$1,000 or more.

20 A rule similar to the rule of the preceding sentence
21 shall apply to any other portion of an asset to the
22 extent that separate treatment of such portion is ap-
23 propriate to carry out the purposes of this section.

24 “(2) ASSETS WHICH ARE NOT INDEXED ASSETS
25 THROUGHOUT HOLDING PERIOD.—The applicable in-

1 flation adjustment shall be appropriately reduced for
2 periods during which the asset was not an indexed
3 asset.

4 “(3) TREATMENT OF CERTAIN DISTRIBUTIONS.—A distribution with respect to stock in a
5 corporation which is not a dividend shall be treated
6 as a disposition.

7 “(4) SECTION CANNOT INCREASE ORDINARY
8 LOSS.—To the extent that (but for this paragraph)
9 this section would create or increase a net ordinary
10 loss to which section 1231(a)(2) applies or an ordi-
11 nary loss to which any other provision of this title
12 applies, such provision shall not apply. The taxpayer
13 shall be treated as having a long-term capital loss in
14 an amount equal to the amount of the ordinary loss
15 to which the preceding sentence applies.

16 “(5) ACQUISITION DATE WHERE THERE HAS
17 BEEN PRIOR APPLICATION OF SUBSECTION (a)(1)
18 WITH RESPECT TO THE TAXPAYER.—If there has
19 been a prior application of subsection (a)(1) to an
20 asset while such asset was held by the taxpayer, the
21 date of acquisition of such asset by the taxpayer
22 shall be treated as not earlier than the date of the
23 most recent such prior application.

(c) EFFECTIVE DATE.—The amendments made by this section shall apply to dispositions after December 31, 2002, in taxable years ending after such date.